



# Turning the Franchise Business Back On

**Leading Your System Out Of Covid-19**

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UPDATES



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INTERNATIONAL FRANCHISE ASSOCIATION

# Speakers



**Kay Marie Ainsley, Managing Director, MSA Worldwide**



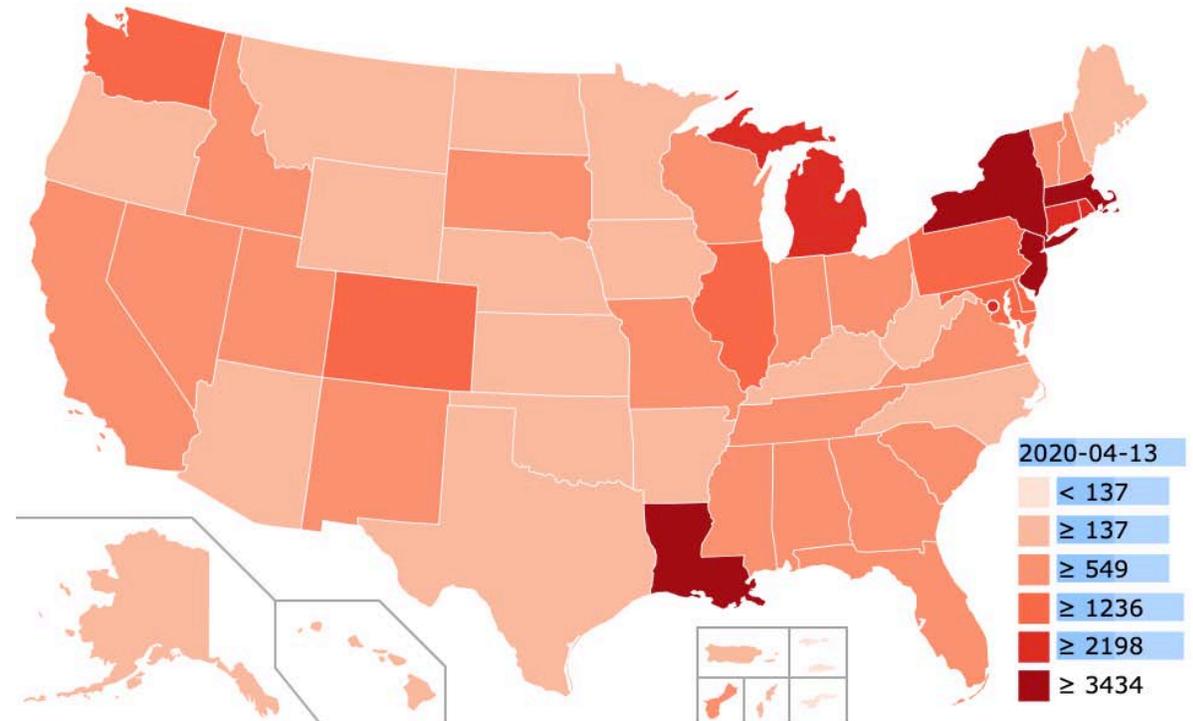
**Michael Seid, Managing Director, MSA Worldwide**

# While the closure has been relatively short

- Franchising will be smaller when it reopens
  - Some locations will not reopen
  - Some locations will open and then soon close
  - Some locations under development will not open as planned
  - Some franchise systems will not survive – sale of systems
  - Multi-unit franchise roll up with incentives

# How the economy will reopen

- Once rapid tests become readily available
  - Rolling by regions impacted
  - Depends on the governors
  - Smaller, more rural, less dense markets
  - Middle of the country first



# Possible regulatory changes

- Disclosure Document – including Item 19
- State registration and capitalization requirements
- Proposed state relationship laws
- Income recognition revisited by FASB
- Covid-19 recommendations become regulations
  - Capacity Control – i.e. 60 seat restaurants to 45 or 30 seats
  - Delivery and pick-up

# Revised FDD Proposal

Event Impact. The COVID-19 Pandemic public health emergency (the “Event”) has affected our Outlets significantly. Our Affiliate Outlets are located in cities with Shelter in Place/Safe at Home orders in effect for the duration of the Event plus an unspecified period of time. Although our Affiliates are allowed to engage in take out and delivery service, Parent has elected to close the Affiliate Outlets until the Event resolves and reopening is appropriate. Because of the COVID-19 Event risk and the unknown impacts on business and consumer behavior, we do not represent or warrant to you in any way that your Franchised Business will be able to open or will be able to stay open after commencing business, or will not suffer any material impairment in its ability to operate.

Joel Buckberg – Baker, Donelson – Nashville, TN

# Revised FDD Proposal

Franchised Outlets. On \*\*\*, 2020, in response to the Event, by means of a policy announcement made a part of the Operations Manual, Franchisor authorized Franchised Outlets to close at their discretion, and announced a royalty holiday during which franchisees are not obligated to pay royalties on gross sales or minimum royalties. We reserved the right to restart your royalty accrual and payment when your Outlet is allowed to reopen with on-premise dining. We may apply that restart on a local basis, when the restrictions lift in each Franchised Outlet's jurisdiction. [Brand Fund discussion].

# Revised FDD Proposal

Operational Changes. As a result of the Event, we may implement through amendment of the Standards in the Operations Manual, temporary or permanent changes in employee uniforms, personal protective equipment, cleaning and sanitation procedures (“Enhanced Procedures”) Standards for each Brand Outlet. These Enhanced Procedures may result in increased costs of labor, materials and supplies for each Brand Outlet. We may also implement Standards changes for packaging of served menu items that may increase costs of labor and operating supplies.

# Revised FDD Proposal

Regulatory Changes. As of the Effective Date, the Event is continuing with no certainty as to the date its immediate impact on the Outlet industry will cease. There are Federal, State and local elements to the regulations arising from the Event that apply to each Franchised Outlet. Each franchisee must comply with the regulations applicable to the Franchised Outlet. Local or state regulations may require more distance between dining seats, which will reduce the on-premise seating available in each Franchised Outlet. Less seating may reduce the number of customers and the revenue of the Outlet. Changes to state and local regulations may adversely affect the operating costs associated with staffing, cleaning and maintaining the Franchised Outlet.

# Revised FDD Proposal

Suspension of Development & Training. During the pendency of the Event, and for any period in which required social distancing requirements effectively prevents development and pre-opening activities (the “Suspension Period”), Franchisee may suspend development activities for the Franchised Outlets it is obligated to develop for the duration of the Suspension Period. Franchisor may likewise curtail or suspend pre-opening services and training until such time as social distancing requirements allow for service delivery for the duration of the Suspension Period. Neither party shall be liable for any increase in cost or damages arising from such delay.

# Revised FDD Proposal

Notice of Event End Date. Franchisor may end the Suspension Period and issue a written notice to Franchisee (the “Restart Notice”) if and when the Federal, state and local restrictions on Outlet operations and on-premise dining applicable to the location of the Franchised Outlet end, and Franchisor believes it can deliver the pre-opening services and training. Within three business days after Franchisee receives that Restart Notice, Franchisee will provide to Franchisor the date on which Franchisee will commence development activity (the “Restart Date”). Franchisee shall resume its development activities and the timeline for performance in the MUDA, if any, and the Unit Agreement, shall be extended by the number of days between the Effective Date and the Restart Date (the “Extension Period”). Franchisor will give Franchisee written notice confirming the number of days in the Extension Period and the resulting timeline changes.

# Revised FDD Proposal

Item 7 Estimates. As of the effective date of the FDD, Franchisor did not have sufficient information to modify the estimated initial investment in a Franchised Outlet for changes in required equipment, suppliers, labor or other circumstances arising from the Event.

# Revised FDD Proposal

Item 19 Disclosure. The Financial Performance Representation in Item 19 is based on the financial performance of fully operational Brand Outlets during 2019 and assumes that such performance provides a reasonable basis for the Financial Performance Representation. No adjustment has been made for the effects of the Event on historical performance. While any Brand Outlet operates without on-premises dining, or with a reduced number of seats for patrons to maintain social distancing, its financial performance may not be comparable to the group whose performance is presented in Item 19. Depending on how long the global pandemic Event continues, its severity in your region, and any unknown, long term impacts on consumer behavior, you could earn substantially less than our 2019 results suggest.

# Revised FDD Proposal

Good Faith Disclosure. Franchisee acknowledges that Franchisor has made a good faith effort to disclose the potential impact of the Event on the franchised business offered in the FDD. The consequences of the Event and any resulting change in business methods of Brand Outlets, System Standards or the finances of Franchisor will not be ascertainable until further development of the Event response by government agencies or until after the Event. The FDD was prepared with information generally available to the public on the Event.

# The recovery demand curve

- Consumer habits and preferences have changed
  - Staycation industries may surge
  - Gatherings in close contact industries will not
  - Virtual interaction will impact travel
- Speed, depth, uniformity of recovery not uniform
- Supply chain, staffing, standards impact

# Short duration but lasting impact on policies

- Inability to sustain short closure
  - Franchisee qualifications
  - Franchisee financing and capital requirements
  - Classes of franchisees to be targeted
  - Use of brokers – virtual recruitment/sales by franchisor
  - Use of 401K plans by franchisees

# Rethinking growth and support

- Virtual discovery days may become a fixture
- Training and opening support
- Field support delivery
- Field support decision making
- Ability to support – geographic growth – critical mass

# Thinking through planning and execution

- Franchising is diverse – even in same industry
  - Size, resources, leadership skills, maturity, customers, economics, franchisee relations
  - Best practices vs contextual practices
  - Execution needs to be nimble with local field decision making in several areas
  - Will require franchisee involvement and trust

# Legal counsel is important but not definitive

- Legal counsel's role is critical in identifying risk
- Management's role is to make business decisions
  - Risk will be unavoidable
  - Franchise agreements are not a good management tool
  - Franchise agreements were never designed for this type of event
  - Trust, moral suasion, communications, franchisee involvement

# Sustainability

- Franchisee sustainability is critical target
- So is franchisor sustainability
  - Reopening costs not budgeted for and will be high
  - Reopening royalties will be lower than before – consumer
  - Initial franchise fees will be slow to recover
- Be aware of financial capabilities before making economic changes

# Franchisee staff retention

- Even with PPP, staff may not return generous U.I.
- Competitive market may increase payroll costs
- Franchisees need to communicate with staff now
- Determine replacement staffing needs
- Factor in expected demand curve

# Training replacement staff

- Training infrastructure insufficient to directly train
- Approaches considered
  - Soft opening
  - Virtual training
  - Train the trainer

# Supply chain

- Disrupted back to farmer and manufacturer
- Anticipate alternatives
  - Products
  - Local sourcing alternatives
  - Limited or alternative menu items
  - Discussions with suppliers – pre-order requirements from franchisees

# Brand standards

- Short term flexibility will be needed
  - Allowing field staff some authority may limit stress
  - Communications to consumers
  - Ensure that everyone knows flexibility is temporary
  - Develop temporary manual – signifies intent to return to standards

# Re-opening tips

- Communicate, communicate, communicate with all audiences
- Evaluate temporary measures for long-term usage
- Renegotiate where possible with suppliers
- Work to regain past customers and retain new customers
- Redeploy corporate resources

# Wrap up

- Unit sustainability is critical target
- Franchisee involvement will garner trust when things don't go as planned
- Field staff authority will allow local flexibility
- Keep communications factual but upbeat
- Don't expect every consumer, franchisee or employee to understand – communications will be critical

# Questions?



# Speakers Contact Information



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